89

(3)

No. 07-929

FILED
MAR 25 2008
OFFICE OF THE CLERK
SUPREME COURT, U.S.

In The
Supreme Court of the United States

DONNA ROSSI and ALBERT MARCO,

Petitioners,

v.

JOSEPH CHRIS PERSONNEL SERVICES, INC.,
Doing Business As Joseph Chris Partners,

Respondent.

On Petition For Writ Of Certiorari
To The United States Court Of Appeals
For The Fifth Circuit

PETITIONERS' REPLY BRIEF

ANDREW S. GOLUB*
DOW GOLUB BERG & BEVERLY, LLP
8 Greenway Plaza
14th Floor
Houston, TX 77046
(713) 526-3700

ERIC SCHNAPPER
University of Washington
School of Law
P.O. Box 353020
Seattle, WA 98195
(206) 616-3167

**Counsel of Record*

Counsel for Petitioners

COCKLE LAW BRIEF PRINTING CO. (800) 225-6964
OR CALL COLLECT (402) 342-2831

TABLE OF CONTENTS

Page

I. There Is A Widely-Recognized Inter-Circuit Conflict Regarding When A Party Waives the Right to Arbitration by Litigating That Claim 1

II. This Case Presents An Appropriate Vehicle for Resolving the Question Presented 8

Conclusion 11

TABLE OF AUTHORITIES

Page

CASES:

Cabinetree of Wisconsin, Inc. v. Kraftmaid Cabinetry, Inc., 50 F.3d 388 (7th Cir. 1995)....*passim*

Galion Iron Works v. J.D. Adams Mfg. Co., 128 F.2d 411 (7th Cir. 1942)..... 8

Keytrade USA, Inc. v. AIN Temouchent M/V, 404 F.3d 891 (5th Cir. 2005)..... 3

National Foundation for Cancer Research v. A.G. Edwards & Sons, Inc., 821 F.2d 772 (D.C. Cir. 1987)..... 1

Rosenthal v. Great Western Financial Securities Corp., 926 P.2d 1061 (Cal. 1996)..... 5

Saint Agnes Medical Center v. PacifiCare of California, 82 P.3d 727 (Cal. 2003)..... 5

Sauer-Getriebe KG v. White Hydraulics, Inc., 715 F.2d 348 (7th Cir. 1983)..... 7, 8

Tenneco Resins, Inc. v. Davy Int'l, 770 F.2d 416 (5th Cir. 1985)..... 3

Tristar Financial Ins. Agency, Inc. v. Equicredit Corp. of America, 97 Fed. Appx. 462 (5th Cir. 2004)..... 3

WorldSource Coil Coating, Inc. v. McGraw Construction Co., 946 F.2d 473 (6th Cir. 1991)..... 6

TABLE OF AUTHORITIES – Continued

Page

OTHER AUTHORITIES:

1 Domke on Commercial Arbitration § 23:8 (2007) 6

I. THERE IS A WIDELY-RECOGNIZED INTER-CIRCUIT CONFLICT REGARDING WHEN A PARTY WAIVES ITS RIGHT TO ARBITRATION BY LITIGATING THAT CLAIM

Three federal appellate decisions, five federal district court decisions, and nine state court decisions have all independently concluded that there is an inter-circuit conflict regarding when a party waives its right to arbitrate by initiating or engaging in litigation about the matter it could instead have arbitrated. (Pet. 27-32). Those seventeen conclusions, written or joined by more than sixty federal and state judges, are quite correct.

Respondent insists that all the federal circuits have adopted the identical legal standard; it contends in particular that the standard in the Fifth Circuit is exactly the same as the standards in the Seventh and District of Columbia Circuits. In the Fifth Circuit "prejudice . . . is the essence of waiver." (Pet. App. 6a) (*quoting Miller Brewing Co. v. Fort Worth Distrib. Co.*, 781 F.3d 494, 497 (5th Cir. 1986)). In the Seventh Circuit "[t]o establish a waiver of the contractual right to arbitrate, a party need not show that it would be prejudiced." *Cabinetree of Wisconsin, Inc. v. Kraftmaid Cabinetry, Inc.*, 50 F.3d 388, 390 (7th Cir. 1995). In the District of Columbia Circuit "waiver may be found absent a showing of prejudice." *National Foundation for Cancer Research v. A.G. Edwards & Sons, Inc.*, 821 F.2d 772, 777 (D.C. Cir. 1987). Respondent offers no account of how these manifestly conflicting

holdings could possibly embody the same legal standard.

Respondent asserts that the Fifth and Seventh Circuits' standards involve what Respondent characterizes as the same three "steps." Both circuits, according to Respondent, (a) "ask" whether the party seeking arbitration took litigation steps inconsistent with an intent to arbitrate, (b) "ask" whether the party seeking arbitration lacks a "valid reason for changing the forum," and (c) "ask" whether the party opposing arbitration was prejudiced by the tactics of the other party. (Br. Op. 11-12, 15). However, because the Fifth and Seventh Circuits attach very different significance to these factors, their standards are patently inconsistent. In the Fifth Circuit a waiver is found only if *all* of these questions are resolved against the party seeking arbitration; in the Seventh Circuit a waiver is found if *any* of these questions is resolved against the party seeking arbitration. A showing of prejudice is essential in the Fifth Circuit because without it not all three factors would support a waiver; a showing of prejudice, on the other hand, is not required in the Seventh Circuit because a finding in support of waiver on either of the other issues would be dispositive. That is why under Seventh Circuit law a finding of prejudice is not required in "normal[ ]" cases. *Cabinetree of Wisconsin, Inc.*, 50 F.3d at 391. In fact, the Seventh Circuit considers prejudice relevant only in "abnormal" and "extraordinary" circumstances. *Id.* at 391. Even in such exceptional cases (when neither other factor requires a

waiver), prejudice is still only a factor that would "weigh" in the decision, and is not, as in the Fifth Circuit, a necessary element of waiver. *Id.*

The Seventh Circuit will find a waiver if the party seeking arbitration failed to exercise "diligence . . . [in] seeking arbitration." *Cabinetree*, 50 F.3d at 390-91. Thus, if that party contends it filed suit merely to seek a determination of arbitrability, the party must have done "all it could reasonably have been expected to do to make the earliest feasible determination of whether to proceed judicially or by arbitration." *Id.* Respondent insists that the Fifth Circuit "asks" if "that party failed to act diligently." (Br. Op. 12). But, there is no such rule in the Fifth Circuit. The case Respondent cites for this proposition – *Keytrade USA, Inc. v. AIN Temouchent M/V*, 404 F.3d 891, 897 (5th Cir. 2005) – says nothing whatsoever about diligence. Indeed, the Fifth Circuit has held that a party could litigate a case for as long as two years without waiving its right to arbitration. *Tenneco Resins, Inc. v. Davy Int'l*, 770 F.2d 416, 420-21 (5th Cir. 1985). Even the most indulgent Fifth Circuit judge would not characterize as "diligent" a party responsible for such a multi-year delay. The Fifth Circuit routinely tolerates such behavior because in that circuit "[d]elay by itself falls short of establishing waiver." *Tristar Financial Ins. Agency, Inc. v. Equicredit Corp. of America*, 97 Fed. Appx. 462, 464 (5th Cir. 2004).

Respondent asserts that, just as the Fifth Circuit "asks" whether there was prejudice, the Tenth and

District of Columbia Circuits "look" at whether prejudice resulted. (Br. Op. 20-21). In context, though, "asks" and "look" have very different meanings, depending on each circuit's distinct test. In the Fifth Circuit a court must indeed "ask" if prejudice occurred, but it cannot find waiver unless the answer is "yes." In the Tenth Circuit, by contrast, prejudice is one of more than a dozen factors a court must "look" at, none of which are dispositive of the waiver question. Thus, the Tenth Circuit has repeatedly found waiver in the absence of prejudice. (Pet. 23-24). And in the District of Columbia Circuit a court may inquire whether there would be prejudice, but is not required to do so; thus, courts there can find waiver even though they did not uncover, or even look for, any prejudice. (Pet. 21-22).

As we noted in the Petition, the highest courts in five states hold that whether litigation in state court waives the right to arbitrate is a matter of federal law; four states hold, to the contrary, that it is a state law issue. (Pet. 25-26 and n.25). If, as the Fifth Circuit has repeatedly insisted, the Federal Arbitration Act mandates a particular waiver standard, then the FAA would control that issue in state court as well. In this respect the Fifth Circuit decision conflicts with the state court decisions treating this as a matter of state law. Respondent deals with this multi-faceted conflict as follows:

> The state courts will be *guided* by the above consistent analyses *when* federal law applies.

> *E.g., Saint Agnes Medical Center v. PacifiCare of California*, 82 P.3d. 727, 732-38 and n.4 (Cal. 2003). These same courts will *look to* their respective state law to answer the arbitration-waiver issue under each respective state law. *Id.*

(Br. Op. 22) (Emphasis added). Respondent apparently contends that all state courts adhere to the same view regarding the FAA's impact, a view which goes something like this: (a) the FAA only matters "when federal law applies," whenever that may be, (b) even if the FAA "applies," federal law only "guides," but does not control, the state courts, (c) state courts "look to" state law (which may or may not mean those courts have to apply what they find), and (d) if the "look[ed] to" state law and the "guid[ing]" federal law are different, the answer is unclear.

No state court has adopted this perplexing approach. In California, so long as the underlying transaction was in commerce – as virtually all transactions are – the FAA controls, period. *Saint Agnes Medical Center*, 82 P.3d at 731 ("[T]he FAA generally preempts any contrary state law regarding the enforceability of arbitration agreements."); *Rosenthal v. Great Western Financial Securities Corp.*, 926 P.2d 1061, 1066 (Cal. 1996) ("because the transactions here involved interstate commerce, questions concerning the arbitrability of the parties' dispute are governed by the [F]AA."). Meanwhile, the state Supreme Courts in Alaska, Arizona, Colorado and Florida

insist, to the contrary, that the waiver standard is governed by state law, not federal. (Pet. 26-27 n.25).

If, as the Fifth Circuit held, the FAA mandates the waiver standard adopted by that circuit, then the state court decisions applying a different standard are wrongly decided. In Illinois, for example, the actions of Respondent in filing the instant action would unquestionably result in a waiver. *WorldSource Coil Coating, Inc. v. McGraw Construction Co.*, 946 F.2d 473, 477 (6th Cir. 1991) ("Under Illinois law . . . [t]he key factor in determining whether a right to compel arbitration has been waived is the type of issues submitted to the court."). In *WorldSource*, as here, the plaintiff argued that it had not waived arbitration by filing suit because its complaint included a request for preliminary injunctive relief. The Sixth Circuit rejected that argument, holding that the plaintiff had waived its right to arbitration because the plaintiff's complaint was not limited to such narrow, preliminary relief. "McGraw's state court complaint requested more than such emergency relief. A complaint for compensatory and punitive damages goes far beyond 'interim or conservatory' relief and raises issues that . . . are arbitrable issues for which no emergency existed." *Id.* at 478. "Seeking relief beyond that required by the emergency . . . would constitute a waiver." *Id.* at 477. "[U]nder Illinois law, it is not necessary for WorldSource to show prejudice." *Id.*; *see* 1 *Domke on Commercial Arbitration* § 23:8 (2007) ("Ordinarily, the filing of a

suit seeking injunctive relief, while pursuing arbitration, does not constitute a waiver of arbitration. However, where the party seeks relief beyond that necessary to maintain the status quo prior to arbitration, waiver may be found.") (footnotes omitted).

Respondent argues that this is one of those "abnormal" and "extraordinary" cases in which the Seventh Circuit would consider prejudice relevant. Respondent, like the court below, asserts that even under Seventh Circuit law the actions in the instant case would not constitute a waiver because the complaint included a request for preliminary injunctive relief. (Br. Op. 1; Pet. App. 12a). In their view, so long as a complaint includes such a request, a plaintiff in the Seventh Circuit may without waiver *also* include in the complaint, and seek to litigate, a claim seeking a judicial determination of the merits of the arbitrable dispute. (Br. Op. 16; Pet. App. 12a). These arguments clearly misstate the rule in the Seventh Circuit. In *Sauer-Getriebe KG v. White Hydraulics, Inc.*, 715 F.2d 348 (7th Cir. 1983), on which Respondent relies, the plaintiff carefully and narrowly limited its lawsuit to a request for preliminary relief "'until such time as the respective rights of the parties under the agreement are determined' by arbitration." 715 F.2d at 349. It was precisely because the plaintiff in *Sauer-Getriebe* did not seek relief on the merits that its filing of suit did not constitute a waiver. *Sauer-Getriebe* reconfirmed two earlier decisions in that circuit which expressly held that commencing suit on the merits of a claim constitutes a

waiver of any right to arbitrate that claim. *Sauer-Getriebe*, 715 F.2d at 350 n.1, citing *United States v. Bregman Construction Co.*, 256 F.2d 851, 854 (7th Cir. 1958) (filing suit on the merits of a claim is "indeed a repudiation of the plaintiff's own promise to arbitrate; it gave the defendant an election, taking the plaintiff at his word, to put an end to the arbitration clause."), and *Galion Iron Works v. J.D. Adams Mfg. Co.*, 128 F.2d 411, 413 (7th Cir. 1942) ("Commencement of a suit in court rather than reliance upon arbitration, with answer by the opposing party upon the merits, is a waiver of the right to arbitrate."). Because the lawsuit filed by Respondent in the instant case sought relief on the merits, and not only (or even primarily) preliminary injunctive relief, it would constitute a waiver under Seventh Circuit law.

II. THIS CASE IS AN APPROPRIATE VEHICLE FOR RESOLVING THE QUESTION PRESENTED

This case presents an appropriate vehicle for resolving a longstanding and widely-recognized dispute among federal and state courts regarding the standard for determining when litigation participation results in a waiver of the right to arbitrate.

In the instant case the plaintiff filed suit seeking a decision on the merits of the very claims it later decided it would rather arbitrate. Unlike *Sauer-Getriebe*, the initial pleading in this action emphatically was not limited to injunctive relief intended

merely to maintain the status quo pending arbitration. Respondent asked the Texas state court to decide its claims on the merits, and it sought all the traditional forms of legal and equitable relief. Even then, the injunctive relief sought was not limited to the period before an arbitrator – if one were ever sought – could hear the matter. Respondent correctly notes that the parties had agreed that either could seek preliminary injunctive relief without waiving the right to arbitrate, but that agreement clearly did not permit a party to sue in court – as Respondent did here – for damages, contractual reformation, and "all other available legal, equitable, statutory, general, specific, whole or partial relief." (*See* Pet. 3, quoting Respondent's original pleading, p. 19).

The Seventh Circuit, applying a standard squarely at odds with the Fifth Circuit's, insists that a party's "[s]election of a forum in which to resolve a legal dispute should be made at the earliest possible opportunity in order to economize on the resources, both public and private, consumed in dispute resolution." *Cabinetree*, 50 F.3d at 391. Respondent's conduct in the instant case would constitute a waiver in the Seventh Circuit because "the earliest possible opportunity" at which Respondent could have selected the forum in which to resolve its claim was *before* it ever filed suit in state court to enforce those claims.

Respondent's lawsuit was not an action to compel arbitration. Its otherwise exhaustive prayer for relief made no mention of an order requiring arbitration. Respondent never filed in state or federal court any

motion to compel arbitration, and in fact demanded a jury trial shortly after Petitioners removed the case to federal court. Tellingly, though Respondent's original pleading mentioned the existence of an arbitration agreement, that pleading neither asked for arbitration nor asserted that arbitration was required. In the conspicuous absence of any demand for arbitration, of course, arbitration was not required.

In sum, this is precisely the type of case in which the waiver standard is of controlling importance. The Fifth Circuit expressly permits a party to dabble at litigation for months or even years, to engage in discovery to test the strength of its claims, and then simply to change its mind, unilaterally withdraw the case from federal court, and start over before a possibly more favorably disposed arbitrator. Other circuits and state courts, by contrast, do not tolerate that sort of manipulation of the trial courts' dockets. Courts outside the Fifth Circuit understand that

> the intention behind [arbitration] clauses, and the reason for judicial enforcement of them, are not to allow or encourage the parties to proceed, either simultaneously or sequentially in multiple forums.

Cabinetree, 50 F.3d at 390. It is hardly surprising that in the Fifth Circuit, which holds a particularly indulgent view of such tactics, district judges have repeatedly balked at the resulting misuse of their time. (Pet. 36-37 n.27).

Certiorari should be granted to resolve this inter-circuit and federal-state court conflict, and to restore the ability of federal district judges to deal with the type of conduct that occurred in this case.

CONCLUSION

For the above reasons, a writ of certiorari should issue to review the judgment and opinion of the Fifth Circuit.

Respectfully submitted,

ANDREW S. GOLUB*
DOW GOLUB BERG &
BEVERLY, LLP
8 Greenway Plaza
14th Floor
Houston, TX 77046
(713) 526-3700

ERIC SCHNAPPER
University of Washington
School of Law
P.O. Box 353020
Seattle, WA 98195
(206) 616-3167

**Counsel of Record*

Counsel for Petitioners